

**BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE**

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REGULATORY AUTH.

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OFFICE OF THE
EXECUTIVE SECRETARY

IN RE: APPLICATION OF MEMPHIS)
NETWORK, LLC FOR A CERTIFICATE OF)
PUBLIC CONVENIENCE AND)
NECESSITY TO PROVIDE INTRASTATE)
TELECOMMUNICATIONS SERVICES)
AND JOINT PETITION OF MEMPHIS)
LIGHT GAS AND WATER DIVISION,)
A DIVISION OF THE CITY OF MEMPHIS,)
TENNESSEE ("MLGW") AND A&L)
NETWORKS-TENNESSEE, LLC ("A&L"))
FOR APPROVAL OF AGREEMENT)
BETWEEN MLGW AND A&L REGARDING)
JOINT OWNERSHIP OF MEMPHIS)
NETWORK, LLC)

DOCKET NO. 99-00909

**REVISED PRE-FILED REBUTTAL TESTIMONY OF
JOHN McCULLOUGH ON BEHALF OF MLGW¹**

Q. PLEASE STATE YOUR NAME, PLACE OF EMPLOYMENT, TITLE AND BUSINESS ADDRESS.

A. My name is John McCullough. I am Vice President of Finance and Secretary-Treasurer of Memphis Light Gas and Water Division, a Division of the City of Memphis, Tennessee. My business address is Memphis Light Gas & Water Division, 220 South Main Street, Memphis, Tennessee 38103.

Q. WHAT DOES YOUR POSITION WITH MLGW ENTAIL?

A. I am responsible for establishing, monitoring and maintaining company-wide financial and administrative objectives, policies, programs and practices which ensure MLGW a continuously sound financial structure. My responsibilities include budget, rates, financial management, cashier, payroll, general accounting, bond issues and investments.

¹ The exhibits filed with the original Pre-Filed Rebuttal Testimony of John McCullough have not been revised. Therefore, copies of these exhibits have not been filed with this Revised Testimony.

- Q. WHAT IS YOUR ROLE IN THE TELECOMMUNICATIONS VENTURE?**
- A.** I was involved in the evaluation of the business plan for this venture and I helped negotiate the operating agreement. I currently serve on the Board of Governors for Memphis Networkx.
- Q. WHAT IS YOUR EDUCATIONAL BACKGROUND?**
- A.** I am a graduate of Auburn University where I received a Bachelor's degree in Electrical Engineering. In addition, I have a Masters of Business Administration degree from Memphis State University. I am a Licensed Professional Engineer in the state of Tennessee.
- Q. PLEASE DESCRIBE YOUR PROFESSIONAL EXPERIENCE.**
- A.** I joined MLGW in 1973 as a Junior Engineer and also served as Assistant and Association Engineer; Construction Schedulers; Supervisor, Budget and Rates; Manager, Budget, Rates and Plant; Manager, Finance and Treasury; and the acting Vice President, Finance and Secretary-Treasurer. In 1998 I became the Vice President, Finance and Secretary-Treasurer.
- Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**
- A.** The purpose of my testimony is to set forth in greater detail the measures that MLGW has already taken in order to prevent subsidy of Memphis Networkx and to set forth the procedures that MLGW intends to put in place if the application and joint petition are approved in this docket. In addition, I will respond to certain statements made by William Barta in the testimony he filed on behalf of the Tennessee Cable Telecommunications Association (TCTA). I will also provide testimony that relates to issues 3, 4, 6, 7, 8 and 9 of the issues list approved by the TRA in this docket.
- Q. WHAT MEASURES HAS MLGW TAKEN TO PREVENT CROSS-SUBSIDIZATION OF MEMPHIS NETWORKX?**
- A.** A subsidy only occurs if MLGW brings to bear its assets and resources for the benefit of Memphis Networkx without proper allocations and/or payment. Memphis Networkx is a separate legal entity from MLGW. MLGW's role in Memphis Networkx is an investor/partial owner. Memphis will have no common employees with MLGW and all transactions with Memphis Networkx will be at arm's length. Attached as Exhibit A to my testimony are the safeguards against cross-subsidy that MLGW and Memphis Networkx have or

will put in place. We believe these safeguards are consistent with the safeguards approved by the TRA in The Chattanooga Electric Power Board Case (Docket No. 97-007488). Although I am not a lawyer, I understand that the FCC's Affiliate Transaction Rules (47 CFR § 32.27) and the structural separation provisions of 47 USC 272(d) are not applicable to MLGW and Memphis Networkx, I have been advised that Exhibit A is consistent with the spirit of those provisions.

Q. WHAT MEASURES HAS MLGW TAKEN TO PREVENT CROSS-SUBSIDIZATION BETWEEN THE TELECOMMUNICATIONS DIVISION AND THE OTHER DIVISION OF MLGW?

- A. Costs that are common to two or more divisions are allocated to the respective divisions through the general ledger system. The system has preset percentages to each division for several thousand charge codes through which all expenditures must pass. For example:

<u>Charge Code</u>	<u>Electric</u>	<u>Gas</u>	<u>Water</u>
Office and clerical labor in the budget department	57%	27%	12%

The percentages are determined by one of several allocation methods based on the number of customers, revenues, or customized formulae. The allocation methods are updated periodically.

A fourth allocation to telecom has been added and a percentage assigned for several employees' labor and for disbursements. The percentage can of course be 100% to a division if appropriate.

Q. Does MLGW have an incentive to subsidize Memphis Networkx?

- A. No.

Q. PLEASE RESPOND TO MR. BARTA'S TESTIMONY ON PAGE 7, LINE 23 THROUGH PAGE 8 LINE THREE IN WHICH HE INDICATES THAT "...THE REGULATED UTILITY SIMPLY DOES NOT HAVE THE INCENTIVE TO MINIMIZE ITS COST."

- A. First, to the extent that Mr. Barta believes this statement relates to MLGW and Memphis Networkx his initial premise is in error. Mr. Barta indicates on page 8, line 21 through 23 that Memphis Networkx is MLGW's "non-regulated telecommunications venture". This is not accurate. Memphis Networkx will be subject to regulation by the TRA. Second, contrary to Mr. Barta's opinion,

MLGW has every incentive to minimize its cost in the provision of electric as well as gas and water services. Certain MLGW utility services may be subject to little or no competition, however, the threat of deregulation and competition is an incentive to lower costs. In actuality, MLGW's operational practices and policies have translated into MLGW having the lowest combined residential utility rates in the country. In the last six years, our combined utility budgets have had a near zero percent increase, which demonstrates that we have both kept our costs down in addition to absorbing inflation. MLGW hopes that their share of revenues from this venture will enable them to reduce their current electric utility rates (after repayment of all loans received from the Electric Division). Third, even if MLGW's services were not subject to competition it would have no incentive to subsidize the operation of Memphis Networkx, because Memphis Networkx is not a wholly owned subsidiary of MLGW. Since Memphis Networkx is partially owned by another entity a percentage of any subsidy would inure to the benefit of A&L, not to MLGW.

[Question and Answer struck pursuant to Pre-Hearing Officer's April 28, 2000 Order]

[Question and Answer struck pursuant to Pre-Hearing Officer's April 28, 2000 Order]

Q. PLEASE COMMENT ON MR. BARTA'S TESTIMONY REGARDING THE NEED FOR A FORMAL SET OF TERMS AND CONDITIONS GOVERNING AFFILIATE TRANSACTIONS BETWEEN MEMPHIS NETWORKX AND MLGW.

A. Mr. Barta states on page 9, line 10 of his testimony that "Based upon my discussions with company representatives and the responses to discovery, there did not appear to be a need for a formal set of terms and conditions governing the affiliate transactions between Memphis Networkx and the utility divisions of MLGW."

Mr. Barta appears to be saying that if we do what we say we are going to do in our testimony and responses to the data requests, then no formal set of terms and conditions governing affiliate transactions need be adopted by the Authority. However, Mr. Barta states that he does not believe that MLGW plans to implement these procedures, based upon the review of numerous documents. The documents that he cites involve various preliminary discussions regarding the telecommunications project, which do not represent MLGW's ultimate decision regarding the form of the telecommunication venture. Mr. Barta has reviewed these documents out of context and has made unreasonable conclusions regarding them.

On November 8, 1999 MLGW and A&L Networks-Tennessee, LLC entered into the umbrella agreement and Operating Agreement which were attached as Exhibit M to the supplemental filing on January 11, 2000, and Exhibit E to the application in this docket, respectively. These are the documents that govern the relationship between MLGW and A&L and described the joint venture. Many things were discussed prior to entering into the operating agreement and the umbrella agreement however, these agreements and the testimony in this docket set forth the current plan and concept for the venture.

Q. WOULD YOU COMMENT ON EACH OF THE DOCUMENTS THAT MR. BARTA LISTS IN HIS MEMO?

A. Yes.

Q. LET'S START WITH WJB-2 IN WHICH MR. BARTA DEALS WITH HIS CONCERN OVER MEMPHIS NETWORKX'S USE OF MLGW'S EXISTING INFRASTRUCTURE. DOES MLGW INTEND TO ALLOW MEMPHIS NETWORKX TO USE ITS EXISTING INFRASTRUCTURE?

A. Memphis Networkx may negotiate use of MLGW's existing infrastructure on an arms length basis just as any other carrier operating in Memphis may do. With respect to pole attachments Memphis Networkx will have to pay the highest rates that MLGW charges to any carrier.

Q. WOULD YOU ADDRESS EACH DOCUMENT THAT MR. BARTA LISTS IN EXHIBIT WJB-2?

A. Except as noted below, I will defer to Wade Stinson who has also filed rebuttal testimony.

1. The April 22, 1990 draft memorandum of understanding - This document is a draft, as indicated in the heading. Arthur D. Little, Inc. ("ADL") drafted this document, however, this draft was never circulated to the city. It was never signed by anybody, nor do we expect it to be signed.

2. September 29, 1999 memo from Michael Kissell to Wade Stinson - Wade Stinson will address with his memo in his testimony.

3. November 25, 1999 enter departmental communication from Mike Kissell - Wade Stinson will address this in his testimony.

4. **A&L Networks LLC December 1, 1998 response to MLGW request for proposal for strategic telecommunications partnership – Wade Stinson will address this in his testimony.**

5. **MSF Network Technology response to MLGW request for proposal for telecommunications strategic partner – Wade Stinson will address this in his testimony.**

6. **BellSouth Business Systems response to MLGW request for proposal for Telecommunication Strategic Partner – Wade Stinson will address this in his testimony.**

7. **March 24, 1999 memo from Erik Wetmore to MLGW Corp. - Wade Stinson will respond to this correspondence in his testimony.**

8. **March 2, 1990 from Joel Havorson of Arthur D. Little to Wade Stinson and Alex Lowe - Wade Stinson will respond to this letter.**

9. **January 6, 1999 proposal of A&L Networks LLC, Arthur D. Little, Inc. and Nortel Networks to MLGW for a Strategic Telecommunications partnership – Wade Stinson will respond to this in his testimony.**

Q. COULD YOU ADDRESS THE DOCUMENTS THAT MR. BARTA REFERS TO IN WJB-3 REGARDING HIS CONCERN OVER MEMPHIS NETWORK ACCESS TO MLGW PERSONNEL AND CUSTOMER INFORMATION?

A. Yes.

Q. WILL MEMPHIS NETWORKX HAVE UNRESTRICTED ACCESS TO MLGW PERSONNEL?

A. Absolutely not. [The remainder of this Answer was struck pursuant to the Pre-Hearing Officer's April 28, 2000 Order.]

Q. WILL MEMPHIS NETWORKX HAVE UNRESTRICTED ACCESS TO MLGW'S CUSTOMER INFORMATION?

A. MLGW's customer information is available to citizens of Tennessee through appropriate requests under the Public Records Act. Memphis Networkx may obtain this information on the same basis as any other person or entity pursuant to MLGW's procedures for requesting such information.

Q. PLEASE COMMENT ON EACH OF THE DOCUMENTS SET FORTH IN WJB-3.

A. Wade Stinson will address all of the documents in WJB-3.

Q. WILL YOU COMMENT ON THE DOCUMENTS SET FORTH IN WJB-4 REGARDING MR. BARTA'S CONCERN REGARDING MLGW NAME RECOGNITION?

A. Wade Stinson will address the documents mentioned in WJB-4.

Q. WILL MEMPHIS NETWORKX USE THE MLGW NAME?

A. The telecommunication services provided by the joint venture between MLGW and A&L Networks Tennessee, LLC will be provided under the name of Memphis Networkx. The ownership of Memphis Networkx will be freely disclosed.

Q. WILL YOU COMMENT ON THE EXCERPTS FROM DOCUMENTS THAT MR. BARTA HAS PROVIDED IN WJB-5?

A. Yes.

Q. HAS MLGW EMPLOYED FACILITIES ON BEHALF OF MEMPHIS NETWORKX WITHOUT RECEIVING PROPER APPROVAL FROM THE TRA?

A. No.

Q. WILL YOU RESPOND TO THE EXCERPTS FROM THE DOCUMENTS LISTED IN EXHIBIT WJB-5?

A. Yes.

1. June 1 1999 letter from Alex Lowe to Wade Stinson and Larry Thompson - Wade Stinson will respond to this letter.

2. April 1, 1999 letter from Alex Lowe form J. B. Hollingsworth General Manager, BellSouth Telecommunications - Wade Stinson will respond to this letter.

3. May 24, 1999 meeting notes - Wade Stinson will respond to this letter.

4. **September 29, 1999 memo from Michael Kissell to Wade Stinson**
- Wade Stinson will respond to this memo.

5. **October 1999 agreement between MLGW and A&L Networks Tennessee to establish a joint venture to provide telecom services** - I don't know what point Mr. Barta is trying to make with this document however, it is an unexecuted draft of the umbrella agreement. The executed document is dated November 8, 1999 and was filed in this docket as Exhibit M to the supplement to the application.

Q. WILL MR. STINSON RESPOND TO WJB-6?

A. Yes.

Q. MR. BARTA STATES THAT HE IS DISTURBED BY "THE COMPANIES' EFFORTS TO RESTRICT DISCLOSURE OF INFORMATION AND MATERIAL THAT WOULD PERMIT AN OBJECTIVE REVIEW OF ITS OPERATIONS AND AFFILIATE TRANSACTIONS." PLEASE RESPOND TO THIS.

A. MLGW has not sought to restrict such disclosure. The memos that Mr. Barta cites in his exhibits are excerpts from approximately 5,000 pages of documents that MLGW produced pursuant to a public records request from John Farris, counsel for TCTA and Time Warner and from responses to discovery requests in this proceeding. [The remainder of this Answer was struck pursuant to the Pre-Hearing Officer's April 28, 2000 Order.]

Q. PLEASE RESPOND TO THE STATEMENT REGARDING THE MEETING NOTES ON PAGE 14, LINES 10-18 OF MR. BARTA'S TESTIMONY.

A. It is my understanding that the notes referenced on page 14 of Mr. Barta's testimony were prepared by an intern from ADL during a brainstorming meeting set up by ADL, at which I was present, which occurred in July, 1999. [The next sentence was struck pursuant to the Pre-Hearing Officer's April 28, 2000 Order.] There was never any discussion as to "slipping" the budget through the Board. The December date appears to reference the date the city council passed the budget. Our expenditures, like all capital expenditures, were included as line items in the approved budget. [The last sentence was struck pursuant to the Pre-Hearing Officer's April 28, 2000 Order.]

Q. WHAT REQUIREMENTS, IF ANY, ARE NECESSARY TO ENSURE THAT STARTUP EXPENSES ALREADY INCURRED BY MLGW ARE CORRECTLY IDENTIFIED AND PROPERLY ALLOCATED?

A. An accumulation of all expenses relating to telecom for 1999 in the amount of approximately \$2.2 million will be shown as a loss on the Electric Division's 1999 income statement under other income gain or loss equity investment, telecom.

The expenses are comprised of: 1) 50% of the loss on the Memphis Networkx 1999 operating income statement; and 2) an estimate of Electric Division expenses relating to telecom for 1999.

In accordance with MLGW Board Resolutions the Telecom Division will reimburse the Electric Division for the above loss after TRA approval and subsequent inter-division loan of \$20,000,000.

Q. HAVE ANY TAX PAYER FUNDS BEEN USED FOR THE TELECOMMUNICATIONS PROJECT AND IS IT ANTICIPATED THAT ANY TAX PAYER FUNDS WILL BE USED FOR MLGW'S INVESTMENT IN MEMPHIS NETWORKX?

A. No tax payer funds have been used for the telecommunications venture, nor are any going to be used for MLGW's investment in Memphis Networkx. The MLGW Board of Governors has authorized an interdivisional loan of up to \$20 million from the Electric Division to the Telecommunications Division of MLGW. The approval for the initial draw of that loan in the amount of approximately \$5,500,000 has been approved by the Tennessee Comptroller's Office pursuant to the provisions of TCA § 7-52-402(2). A letter of approval dated November 24, 1999 was attached as Exhibit N to our supplemental filing which was made on January 11, 2000. Since the filing of that supplement and the filing of Ward Huddleston's direct testimony, MLGW has sought and obtained a correction to the amount approved from \$5,300,000 to approximately \$5,500,000. The request for the adjustment dated February 3, 2000 and the response approving the request from the comptroller of the treasury dated February 4, 2000 are attached to my testimony as Exhibit B. MLGW intends to seek approval of draws on the \$20 million loan as needed.

The Telecommunications Division intends to make an initial investment of approximately \$5.3 million dollars in Memphis Networkx. The Telecommunications Division will use revenues from Memphis Networkx to pay off the loan.

The funds of the Electric Division that will be loaned to the Telecommunications Division are funds generated by the Electric Division from services provided to electric rate payers. These are not tax payer funds. These funds are now classified as cash reserves of the Electric Division. It should also be noted that both the Umbrella Agreement (page 6, paragraph 10) and the Operating Agreement (Section 14.8, pages 38 and 39) provide that "neither the tax revenues nor the taxing power of the City of Memphis, Tennessee are in any way pledged or obligated under this agreement."

Q. HAS MLGW COMPLIED WITH THE PROVISIONS OF T.C.A. § 7-52-402-405?

A. With respect to T.C.A. § 7-52-402, MLGW is not providing the services directly. MLGW has formed a Telecommunications Division within the Electric Division in order to separate and allocate cost attributable to its investment in Memphis Networkx, telecommunications joint venture. As stated earlier, we have obtained approval from the comptroller from an interdivisional loan, however no funds have been advanced under the loan as we are awaiting TRA approval.

With respect to T.C.A. § 7-52-403(b), as indicated above, MLGW is not providing the service directly. However, it is my understanding that Memphis Networkx does not plan to provide communications services in the territories of incumbent local exchange carriers with less than 100,000 access lines, except as may be allowed by state or federal law. With respect to T.C.A. § 7-52-404 – tax equivalent payments, payments will be based upon revenues that we receive from our ownership interest in Memphis Networkx. Again, MLGW is not providing the services directly. MLGW will continue to comply with Tennessee statutes that proscribe transfers from municipal utilities to the city for in-lieu-of-tax payments. Memphis Networkx will pay all applicable franchise fees.

With respect to T.C.A. § 7-52-405, MLGW will charge Memphis Networkx the highest rate it charges to any person or entity for a comparable pole attachment. MLGW will also charge Memphis Networkx any applicable rights-of-ways fees, charges or payments required by state or local law that it would charge to any other company. [The last sentence was struck pursuant to the Pre-Hearing Officer's April 28, 2000 Order.]

Q. WHAT CONDITIONS, RULES AND/OR REPORTING REQUIREMENTS, IF ANY, ARE NECESSARY TO INSURE COMPLIANCE BY MLGW AND MEMPHIS NETWORKX WITH THE PROVISIONS OF T.C.A. § 7-52-402-405?

A. I do not believe that any condition rules or reporting requirements are necessary to insure compliance by MLGW and Memphis Networkx with the provisions of T.C.A. § 7-52-402-405. I am not a lawyer, however, it is my understanding that some of these provisions are not within the TRA's jurisdiction to enforce. For example, the comptroller must approve our inter-divisional loan and we have to make tax equivalent payments to the City of Memphis. In any event, regardless of the enforcing entity, these requirements are in Tennessee statutes and MLGW intends to comply with the law. If we do not comply with provisions that the TRA has jurisdiction to enforce, this agency has the power to investigate, ask for voluntary compliance and/or issue a show-cause order. We think that this is sufficient to insure compliance.

Q. WHAT CONDITIONS, RULES, OR REPORTING REQUIREMENTS, IF ANY, ARE NECESSARY TO ENSURE APPLICANT'S AND PETITIONERS' COMPLIANCE WITH THE PROHIBITION AGAINST ANTI-COMPETITIVE PRACTICE PROVISION OF T.C.A. § 7-52-103(d)?

A. As stated above, T.C.A. § 7-52-103(d) is the law. MLGW intends to comply with the law. To the extent that the TRA has regulatory authority over our compliance with the law, the TRA has the authority to do investigations and issue show-cause orders, etc., if they believe we are violating the law and order us to comply with it. We believe that is sufficient.

Q. WHAT CONDITIONS, RULES OR REPORTING REQUIREMENTS, IF ANY, ARE NECESSARY TO INSURE APPLICANT'S AND PETITIONERS' COMPLY, TO THE EXTENT APPLICABLE, WITH T.C.A. § 65-5-208(c)?

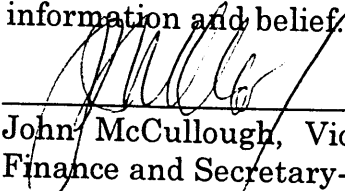
A. I am no lawyer, but I understand there is some question about whether this provision is applicable to MLGW and Memphis Networkx. If it is applicable to us, MLGW is already putting into place structure and practices that will safeguard against anti-competitive practices pursuant to T.C.A. § 7-52-103(d) which should also satisfy T.C.A. § 65-5-208(c). If more is required of us than that, and the TRA tells us what it is, then we will comply with it. Again, no condition, rules or reporting requirements are necessary because we intend to comply with the law and the TRA has the ability to investigate and order enforcement of the law.

Q. DOES THAT CONCLUDE YOUR TESTIMONY?

A. Yes.

VERIFICATION

I, John McCullough, declare under penalty of perjury that I am authorized by Memphis Light Gas & Water Division to testify on its behalf, that I have caused the foregoing written testimony to be prepared on my behalf, that I have read the foregoing testimony and that the statements contained therein are true and correct to the best of my knowledge, information and belief.



John McCullough, Vice President of
Finance and Secretary-Treasurer of
Memphis Light Gas Water Division

STATE OF TENNESSEE)

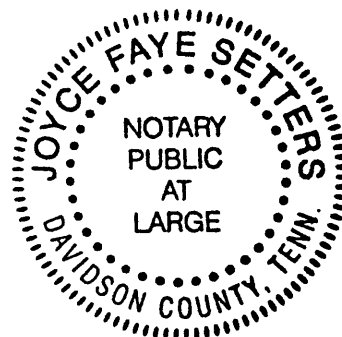
COUNTY OF SHELBY)

Sworn to and subscribed before me this 1 day of May, 2000.



Notary Public

My Commission Expires: Sept 29, 2001



My Commission Expires Sept 29, 2001